

# BANKRUPTCY



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This brochure is intended to be an overview of common issues relating to bankruptcy. It is intended to provide general guidance only and not as a full explanation of the bankruptcy process. It should not be used as a substitute for the advice of an attorney. Rather, use this pamphlet to assist you in sorting through the issues as you determine whether bankruptcy is right for you.

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There is an increasing trend nationwide in the area of consumer bankruptcy filings. While corporate filings have remained relatively unchanged during the last 20 years, individual bankruptcy filings have increased roughly five-fold.

#### *Bankruptcy in General:*

Under federal law, bankruptcy allows a person who cannot meet his or her financial obligations to have those obligations forgiven or reorganized. It protects people who owe debts from the people to whom the debts are owed until those debts are discharged or reorganized.

A bankruptcy filing may adversely impact your personal credit. A bankruptcy can appear on your credit record for 10 years. But, since bankruptcy wipes out your old debts, you are likely to be in a better position to pay your current bills, and you may be able to get new credit.

Because bankruptcy is a matter of federal law, it is handled by federal courts, which, unlike state courts, may or may not be in the county in which you live. Therefore, if you intend to seek bankruptcy protection, you should find the federal court nearest you.

In Texas, there are four federal judicial districts: the Northern, the Eastern, the Southern, and the Western. To find the bankruptcy court nearest you, you may visit the federal court locator website at <http://vls.law.vill.edu/Locator/fed-court.html>.

#### *Why File for Bankruptcy Protection:*

Through a bankruptcy, you may be able to:

- “Discharge” most or all of your debts. In other words, you may be able to avoid paying most or all of your debts. This is to allow an opportunity for a new start.
- Prevent foreclosure on your property, eviction, or repossession of your car. This is a temporary measure, however, and you will be required to keep making payments if you want to keep the property. Bankruptcy is not a means by which to keep property while avoiding payment.

- Prevent harassing debt collection actions by the people or companies you owe.
- Prevent having your utilities cut off. Also, if your utilities have been cut off, you may be able to have them restored.
- Challenge people or companies who have defrauded you or who are overreaching in their debt collections.

### *Bankruptcy is No Cure-all*

Bankruptcy will not solve all of a person's financial problems, and it is not right for everyone. Bankruptcy will not:

- Overcome the claims of secured creditors. A secured creditor is one who possesses a lien, or security interest, in the property for which money was borrowed. In such cases, the property is called "collateral", and can be taken if the underlying debt is not paid. So, it is usually necessary to continue making payments on underlying debts. You generally cannot keep the collateral unless you keep making payments on the debt.
- Overcome certain types of obligations. These include child support, alimony, certain other debts related to divorce, some student loans, court restitution orders, criminal fines, and some taxes.
- Overcome claims against co-signers on your debts. If other people signed to help you get a loan, and you discharge the loan in bankruptcy, the person who signed may still be responsible for the loan.
- Overcome claims for new debts. In other words, a bankruptcy will not protect a person from debts incurred after the bankruptcy.

### *Choosing the Right Type of Bankruptcy*

One of the early steps in filing for bankruptcy involves choosing the type of bankruptcy that is best suited to your particular needs. You may have heard these types of bank-

ruptcy referred to by their respective chapter numbers. The two most common types of bankruptcy are Chapter 7 and Chapter 13 bankruptcies. Chapter 7 requires a debtor to give up non-exempt property, which is then sold to pay creditors. Chapter 7 bankruptcies are sometimes called “liquidation bankruptcies.” Chapter 13 requires repayment of debts, or parts of debts, from income. It is sometimes called “debt adjustment.” Other types of bankruptcies include Chapter 12, for family farmers, and Chapter 11, which provides for relatively complex debtors. Chapter 11 is seldom appropriate for an individual’s bankruptcy.

### *Chapter 7*

Under Chapter 7, the person seeking bankruptcy protection files a petition asking the court to discharge his or her debts. This type of bankruptcy offers the discharge of debts in exchange for the surrender of non-exempt property. Many categories of property are exempt, but non-exempt property is sold and the proceeds are distributed to creditors. Determination of whether particular property is exempt is complex, and should be done in consultation with an attorney. Moreover, you may not be able to keep typically exempt property like a home or a car if you are behind on the home loan or car loan payments. That is because lien holders may still recover their collateral unless you agree to continue, and actually continue, making payments.

### *Chapter 13*

Under Chapter 13, the debtor develops a plan to pay off some of his or her past-due and current debts over three to five years. Chapter 13 allows the debtor to keep valuable property – especially a home and car, which might otherwise be repossessed or foreclosed upon. But, the debtor will be required to make payments to his or her creditors. Usually, such payments will equal or exceed the payments previously faced by the debtor, because an extra sum is added to help reduce the delinquent amount.

Chapter 13 may be well suited to debtors who wish to protect valuable property that is not exempt and who can afford to pay their creditors over a 3 to 5 year period. It also may be well suited to debtors who are behind on payments, but who are not so far behind as to be unable to catch up. Chapter 13

is not well suited to debtors who cannot afford to pay for essential expenses, like living expenses, in addition to the required payments as they come due under the plan.

### *The Cost of Bankruptcy*

There are various costs associated with filing for bankruptcy. It now costs \$200 to file for a chapter 7 and \$185 to file for a chapter 13. The court may allow you to pay this filing fee in installments if you cannot pay all at once. If you choose to hire an attorney, extensive legal fees may also be incurred.

### *What Property Can a Bankrupt Debtor Keep?*

Bankruptcy does not change your right to get many federal benefits, including Social Security, V.A. benefits, and welfare. Plus, under Texas law, you are allowed to exempt, or protect from the bankruptcy, a number of other types of property.

One type of property that a person may protect from creditors during a bankruptcy in Texas is his or her homestead. This protection is unlimited in value, however there are certain restrictions on the size of the real estate to be protected; the property may not exceed ten acres in an incorporated town, village, or city and may not exceed 100 acres for an individual person, or 200 acres for a family outside of an incorporated town, village or city.

In addition to this protection for real property, a person may protect certain personal property. This may include athletic and sporting equipment, including bicycles; two firearms; home furnishings, including family heirlooms; food; clothing; jewelry, one wheeled motor vehicle per family member or single adult who holds a driver's license (or who operates vehicle for someone else who does not have a license); two horses, mules or donkeys, and a saddle, blanket and bridle for each; twelve head of cattle; 60 head of other livestock; 120 fowl; and pets. Property protected by this personal exemption may not be valued at more than \$30,000, or \$60,000 for the head of a family.

There are a few important rules to remember in determining whether property is exempt. First, the value of property is not the amount a person paid for it, but what the property is

presently worth. Many types of property, especially cars, may depreciate quickly, dramatically affecting the ultimate value of the property.

Second, a person should evaluate his or her equity in property. For example, if a person owns a \$4,500 automobile and has \$4,000 left to pay on the note, that person has \$500 in equity in the automobile. It is the \$500 that counts against the personal property cap, not the total value of the automobile. That means, if the debtor can keep paying the regular payments on the automobile, he or she will not need to sell it to pay creditors. This is true even though the total value of the automobile exceeds the \$30,000 personal property exemption provided by the Texas Property Code.

Some other exemptions include:

- Certain types of retirement accounts, including Keogh accounts, to the extent that they are tax-deferred; IRAs, to the extent that they are tax-deferred; judges' pensions; firefighters' pensions; county and district employees' pensions; law enforcement officers' survivors pension; municipal employees' pension; police officers' pension; state employees' pension; teachers' pension; and other retirement benefits, to the extent that they are tax-deferred.
- Certain types of insurance, including church benefit plan benefits; fraternal benefit society benefits; life, health, accident or annuity benefits or money, life insurance present value if beneficiary is debtor or debtor's dependent; retired public school employees group insurance; Texas employee uniform group insurance; and Texas state college or university employee benefits.
- Certain wages, including wages already earned but yet unpaid (except for court-ordered child support), and unpaid commissions not to exceed \$7,500 for an individual or \$15,000 for a family.
- Certain public benefits, including public assistance, medical assistance, unemployment compensation, and workers compensation.



- Certain tools of a trade, including farming and ranching vehicles and implements; tools; equipment; and professional books.

It is important to note, however, that although a person's exemptions allows him or her to keep property even in a chapter 7 case, such exemptions do not impair the right of a purchase lender such as a mortgage company or automobile finance company who has a security interest in a piece of property to take the house or car to cover a delinquent debt on that particular piece of property. Under Chapter 13, a person can keep all of his or her property if he or she follows the court-approved plan. In most cases a debtor will have to pay the mortgages or liens just as the debtor would without the bankruptcy.

#### *How are Other Ownership Rights Affected by Bankruptcy?*

There is a common misperception that a bankrupt debtor cannot own anything for a period of time after filing for bankruptcy. A bankrupt debtor can keep his or her exempt property and anything he or she acquired after the bankruptcy is filed. However, if a bankrupt debtor receives a windfall by way of an inheritance, a property settlement, or life insurance benefits within 180 days after filing for bankruptcy, that money or property may have to be paid to his or her creditors if the property or money is not exempt.

#### *What Happens at the Courthouse?*

In most cases, a bankrupt debtor will only need to go to court for what is referred to as the "meeting of creditors". This is to meet with the bankruptcy trustee and any creditor who chooses to come. Most of the time, this meeting will be a short and simple procedure where the bankrupt debtor is asked a few questions about his or her bankruptcy forms and financial situation.

However, a court appearance may be necessary. If you need to go to court, you should receive notice of the court date and time from the court and/or from your attorney.

#### *Will Bankruptcy Clear all Debts?*

Bankruptcy will clear many debts, but it will not normally clear: debts owed for child support or alimony, fines, and

some taxes; debts not listed on a debtor's bankruptcy petition; loans obtained by a debtor by knowingly giving false information to a creditor who reasonably relied on it in making the loan; some student loans; mortgages and other liens which are not paid in the bankruptcy case (but bankruptcy will wipe out your obligation to pay any additional money if the property is sold by the creditor); or debts resulting from "willful and malicious" harm (such as damages caused by drunk driving).

#### *Miscellaneous Issues:*

There are many other notable aspects of bankruptcy protection. First, public utilities, like electric and gas providers, cannot refuse or cut off service in response to a bankruptcy. However, the utility company can ask for a deposit for future service and bankrupt debtors do have to pay bills that arise after bankruptcy is filed.

Second, an employer or government agency cannot discriminate against a person on the basis of his or her having filed for bankruptcy.

Third, if a bankrupt debtor lost his or her driver's license solely for an inability to pay court-ordered damages caused in a traffic accident, bankruptcy will allow the debtor to recover the license.

Co-signers should be aware that if they have co-signed a loan with a person who files for bankruptcy, the co-signer might have to pay the debt.

#### *Is an Attorney Required?*

You need not have an attorney to file bankruptcy. While it may be possible for some people to file a bankruptcy case without an attorney, such an action should not be taken without serious consideration. The process is difficult and a debtor could lose property or other rights without extensive knowledge of the relevant law. Filing for bankruptcy takes patience and careful preparation. Chapter 7 cases are easier. Very few people have been able to successfully file chapter 13 cases on their own.

### *Deciding Whether to File?*

Deciding whether to file for bankruptcy protection is a complex individual decision involving numerous considerations. There are many different reasons to file, and as many different reasons to not file. If a person is unsure, he or she should speak to an attorney for advice. It is important to remember that bankruptcy will not fix everyone's money problems.

In deciding whether to seek bankruptcy protection, you should first make a monthly budget. List, and add up, all of your regular monthly expenses **for necessities**. Include expenses like: rent/mortgage payments, utilities, food, gas or bus fare, clothing, and other regular monthly expenses that you expect to have even after bankruptcy. If you have a car loan and you want to keep the car, include the car payments also. Then add up the monthly income for everyone in the house who shares expenses. Include your job, public benefits, food stamps, pensions, or disability payments.

If your income is a lot less than your expenses, then bankruptcy might not help. Bankruptcy only wipes out old debts. So if your budget shows that you will have trouble making ends meet after bankruptcy, or if you think you will still need to use credit cards or borrow money after filing, then you need to think about getting a second job or cutting expenses (for example, by getting a cheaper car or apartment).

Also look at how old your debts are. Most consumer debts only stay on your credit report for seven years. A bankruptcy will stay for ten years. So, if your debts are a few years old, it might be better to just hang in there for a few more years until they are taken off your credit report and your creditors give up (or until you can pay them).

Again, deciding whether to file bankruptcy is a difficult decision that may require the assistance of an attorney. If you decide that you need help in finding an attorney in your area, you may consult with the Lawyer Referral Information Service online at:

<http://www.texasbar.com/public/findlawyer/lawyerref.asp>

or, call 1-800-252-9690 or 1-877-TEXBAR (toll free).